

**STATE CORPORATION COMMISSION  
RICHMOND, VIRGINIA**

**REPORT ON AUDIT  
FOR THE YEAR ENDED  
JUNE 30, 1999**

***AUDITOR OF  
PUBLIC  
ACCOUNTS***



***COMMONWEALTH OF VIRGINIA***

## **AUDIT SUMMARY**

Our audit of the State Corporation Commission for the year ended June 30, 1999, found:

- proper recording and reporting of transactions, in all material respects, in the Commonwealth Accounting and Reporting System;
- no material weaknesses in internal controls;
- no instances of noncompliance that are required to be reported; and
- adequate implementation of corrective action on the previous year audit findings.

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November 5, 1999

The Honorable James S. Gilmore, III  
Governor of Virginia  
State Capitol  
Richmond, Virginia

The Honorable Richard J. Holland  
Chairman, Joint Legislative Audit  
and Review Commission  
General Assembly Building  
Richmond, Virginia

### INDEPENDENT AUDITOR'S REPORT

We have audited the financial records and operations of the State Corporation Commission (the Commission) for the year ended June 30, 1999. We conducted our audit in accordance with Government Auditing Standards, issued by the Comptroller General of the United States.

#### Audit Objectives, Scope, and Methodology

Our audit's primary objectives were to evaluate the accuracy of recording financial transactions on the Commonwealth Accounting and Reporting System and in the Commission's accounting records, review the adequacy of the Commission's internal control, and test compliance with applicable laws and regulations. We also reviewed the Commission's corrective actions of audit findings from prior year reports.

Our audit procedures included inquiries of appropriate personnel, inspection of documents and records, and observation of the Commission's operations. We also tested transactions and performed such other auditing procedures as we considered necessary to achieve our objectives. We reviewed the overall internal accounting controls, including controls for administering compliance with applicable laws and regulations. Our review encompassed controls over the following significant cycles, classes of transactions, and account balances:

Revenues and Cash Receipts  
Expenses  
Fixed Assets

Accounts Receivable  
Payroll

We obtained an understanding of the relevant internal control components sufficient to plan the audit. We considered materiality and control risk in determining the nature and extent of our audit procedures. We performed audit tests to determine whether the Commission's controls were adequate, had been placed in

operation, and were being followed. Our audit also included tests of compliance with provisions of applicable laws and regulations.

The Commission's management has responsibility for establishing and maintaining internal control and complying with applicable laws and regulations. Internal control is a process designed to provide reasonable, but not absolute, assurance regarding the reliability of financial reporting, effectiveness and efficiency of operations, and compliance with applicable laws and regulations.

Our audit was more limited than would be necessary to provide assurance on internal control or to provide an opinion on overall compliance with laws and regulations. Because of inherent limitations in internal control, errors, irregularities, or noncompliance may nevertheless occur and not be detected. Also, projecting the evaluation of internal control to future periods is subject to the risk that the controls may become inadequate because of changes in conditions or that the effectiveness of the design and operation of controls may deteriorate.

#### Audit Conclusions

We found that the Commission properly stated, in all material respects, the amounts recorded and reported in the Commonwealth Accounting and Reporting System and in the Commission's accounting records. The Commission records its financial transactions on the cash basis of accounting, which is a comprehensive basis of accounting other than generally accepted accounting principles. The financial information presented in this report came directly from the Commonwealth Accounting and Reporting System.

We noted no matters involving internal control and its operation that we consider to be material weaknesses. Our consideration of internal control would not necessarily disclose all matters in internal control that might be material weaknesses. A material weakness is a condition in which the design or operation of the specific internal control components does not reduce to a relatively low level the risk that errors or irregularities in amounts that would be material to financial operations may occur and not be detected promptly by employees in the normal course of performing their duties. The results of our tests of compliance with applicable laws and regulations disclosed no instances of noncompliance that are required to be reported under Government Auditing Standards.

The Commission has taken adequate corrective action with respect to audit findings reported in the prior year.

This report is intended for the information of the Governor and General Assembly, management, and the citizens of the Commonwealth of Virginia and is a public record.

#### EXIT CONFERENCE

We discussed this report with management at an exit conference held on January 20, 2000.

AUDITOR OF PUBLIC ACCOUNTS

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kva:29

## AGENCY BACKGROUND AND FINANCIAL HIGHLIGHTS

The State Corporation Commission (the Commission) is an independent agency directed by three commissioners; each elected by the General Assembly for six-year terms. Each commissioner administers specific divisions and annually the commissioners rotate the chairmanship. The Commission has both regulatory and non-regulatory divisions. The regulatory divisions monitor such industries as utilities, banks, securities, retail franchising, insurance, and corporations. The non-regulatory divisions provide administrative and legal support. The Commission funds its operations from certain regulatory assessments and fees set by statute. The Commission collects revenues for the General Fund, other state special funds, localities, and other entities.

The regulatory and non-regulatory divisions are shown below.

<u>REGULATORY DIVISIONS</u>	<u>NON-REGULATORY DIVISIONS</u>
Insurance	Commissioners Offices
Utilities and Railroad Communications	Commission Comptroller
Economics and Finance	Information Resources
Energy Regulation	General Counsel
Public Service Taxation	Information Technology
Public Utility Accounting	Personnel/Administration
Railroad Regulation	Hearing Examiners
Financial Institutions	
Business Practices	
Clerk's Office	
Securities and Retail Franchising	

### REGULATORY DIVISIONS

Three regulatory groups, Insurance, Utilities and Railroad, and Financial Institutions operate similarly. Each of these groups can set and assess special fees within certain statutory limits to provide operating revenue for the Commission. Insurance and Utilities and Railroad also collect statutorily set taxes and fees from regulated entities and transfer these collections to the General Fund of the Commonwealth or other funds and entities. The Commission may retain any excess operating revenue over expenses. Annually, the commissioners evaluate cash reserves and adjust rates and fees.

Business Practices does not retain any excess cash balances. All collected taxes and fees in excess of operating expenses go to the General Fund of the Commonwealth. The following sections discuss the divisions' operation in more detail.

## Insurance, Utilities and Railroad, and Financial Institutions

The Bureau of Insurance regulates, licenses, and examines insurance companies doing business in Virginia; issues licenses to agents; reviews life, health, and property and casualty policy forms and rates; and helps resolve consumer disputes. The Utilities and Railroad group regulates utility companies by reviewing and setting rates, monitoring utility construction projects, performing gas pipeline safety inspections, auditing financial records, and monitoring financial reporting. The Public Service Taxation Division collects taxes and fees for the Utilities and Railroad group. The Bureau of Financial Institutions regulates and examines state-chartered banks, savings and loans, and credit unions. Financial Institutions also licenses and examines mortgage lenders and brokers, and licenses and regulates money order sellers, consumer finance companies, and debt counseling services.

Below is a summary of financial activity for the year ended June 30, 1999:

	<u>Insurance</u>	<u>Utilities and Railroad</u>	<u>Financial Institutions</u>
Statutorily set taxes collected for:			
General Fund of the Commonwealth	\$245,193,198	\$105,760,931	\$ -
Department of Fire Programs	13,163,600	-	-
Insurance companies (Uninsured Motorist Fund)	5,963,755	-	-
Literary fund	1,127,624	-	35,200
Localities	-	435,030	-
Other	1,168,125	-	-
Total collections for others	<u>266,616,302</u>	<u>106,195,961</u>	<u>35,200</u>
Operating revenue:			
Special assessments, fees, and fines for operations	<u>14,770,312</u>	<u>21,657,682</u>	<u>10,013,520</u>
Operating expenses:			
Salaries and fringe benefits	9,398,703	6,422,234	5,200,143
Indirect charges	400,199	254,126	145,197
Goods and services	7,121,378	4,433,591	2,676,288
Dual party relay	-	7,328,079	-
Travel reimbursements	106,934	46,962	694,122
Debt service payments on Tyler Building	174,438	537,916	331,892
Other	2,260	300,507	-
Total expenses	<u>17,203,912</u>	<u>19,323,415</u>	<u>9,047,642</u>
Net operating increase (decrease) for the year	<u>\$ (2,433,600)</u>	<u>\$ 2,334,267</u>	<u>\$ 965,878</u>
Operating cash balance at June 30, 1999	<u>\$ 8,091,981</u>	<u>\$ 21,654,583</u>	<u>\$ 5,081,878</u>

Salaries and fringe benefits and goods and services represent the majority of the total operating expenses. For Utilities and Railroad, dual party relay payments are a significant expense. One telephone company operates the relay center and the Commission pays that company for operating costs. The Commission collects a monthly surcharge from telephone companies.



Cash balances on hand at June 30, 1999, consist of cash reserves as well as operating cash that will fund operating expenses in the next fiscal year. The Commission has set cash reserve policies equal to six months of operating expenses for Insurance, and three months for Utilities and Railroad. Utilities' large cash balance includes the cash reserve and \$15.8 million in special assessments collected in June 1999, and \$8.3 million for the Dual Party Relay Program that will fund operating expenses next year. The Commission will consider any excess balance when it determines the new special assessment rate in April 2000. Financial Institutions has a cash reserve policy of approximately three months of expenses. The year-end cash balance also includes some of the \$2.5 million in assessments collected late in the fiscal year, which will fund fiscal year 2000 operating expenses.

During fiscal year 1999, in accordance with the Code of Virginia, the Commission began collecting special assessments for the Virginia Department of State Police to investigate insurance fraud. Each licensed insurer doing business in the Commonwealth, by writing any type of property and casualty insurance, except title insurance, pays a special assessment fee equal to a percentage of its direct gross premium income during the preceding calendar year. The Commission can impose a late payment penalty of ten percent of the assessment. The Commission retains a portion of collections to cover its administrative expenses and transferred \$2,987,264 by fiscal year end.

### Business Practices

The Business Practices' divisions register corporations, partnerships, and other companies, as well as trademarks and securities. These divisions collect statutorily set registration and filing fees and withhold a certain amount to cover appropriated operating expenses. The Commission transfers to the general fund any excess withheld over operating expenses. The following is a summary of financial activity for the year ended June 30, 1999.

Total collections	<u>\$ 30,707,413</u>
Deposits to:	
General Fund	5,594,868
Literary Fund	<u>360,797</u>
Total collections for others	<u>5,955,665</u>
Amount retained for operations	<u>24,751,748</u>
Operating expenses:	
Salaries and fringe benefits	4,430,100
Indirect charges	320,191
Goods and services	5,498,920
Travel reimbursements	31,230
Debt service payments on Tyler Building	<u>485,767</u>
Total expenses	<u>10,766,208</u>
Excess of operating revenues over operating expenses	13,985,540
Excess transferred to the General Fund	<u>16,242,388</u>
Net operating decrease for the year	<u>\$ ( 2,256,848)</u>
Operating cash balance at June 30, 1999	<u><u>\$ 9,529,302</u></u>

Beginning in January 1998, corporation registration annual fees became due in a corporation's anniversary month in accordance with Chapter 216 of the 1997 Acts of Assembly. Previously, annual fees for all corporations were due April 1 of each year. The Business Practices cash balance at year-end will fund operating expenses for a portion of the next fiscal year. The Commission transferred the remaining excess balance to the General Fund.

#### NON-REGULATORY DIVISIONS

The non-regulatory divisions provide administrative and legal support for the Commission. The Commission allocates non-regulatory divisions' operating expenses to the regulatory divisions as an indirect charge. The allocation relies upon statistics and percentages calculated every two years. Below is a summary of non-regulatory divisions' expenses for the year:

Personal services	\$ 5,680,099
Goods and services	<u>5,976,297</u>
Total	<u><u>\$11,656,396</u></u>

STATE CORPORATION COMMISSION  
Richmond, Virginia

COMMISSION OFFICIALS

Members of Commission

Theodore V. Morrison, Jr., Chairman

Hullihen Williams Moore

Clinton Miller